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FEI Austin: Accounting & Financial Reporting Update

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MAKING AN IMPACT THAT MATTERS since 1845

Contents

Polling question

Are you a financial statement preparer, user, auditor, or other interested party?

- Preparer
- User
- Auditor
- Other
- Don’t know/not applicable

Joe Biden on tax policy

What’s on the table for tax policy under President Biden?

Business tax proposals

	Current law	Biden proposals
Corporate income	Taxed at 21%	Raise rate to 28% 15% minimum tax on “book” income of companies reporting US net income >$100 million per their financial statements but owe no US income tax per their tax return
Foreign-sourced income of US-based multinationals	Global intangible low taxed income (GILTI) earned by US-based multinationals has an effective tax rate of 10.5% through 2025, then 13.125%	Increase GILTI effective rate to 21% and calculate on a country-by-country basis End provision that allows US companies to “pay nothing on the first 10% of their foreign income” (presumably, eliminate GILTI exemption for QBAI)

Source: Biden for President website; “Biden to target tax-avoiding companies with minimum federal levy,” by Jennifer Epstein, Bloomberg (Dec. 4, 2019); Biden campaign speech, Sept. 9, 2020

What's on the table for tax policy under President Biden?

Business tax proposals

	Current law	Biden proposals
Tax treatment of domestic companies that move jobs overseas or re-domesticate jobs	Anti-inversion regulations and Foreign-Derived Intangible Income (FDII)	Impose 10% "offshoring tax penalty" on profits of foreign production intended for sale back into the US (expected to result in an effective tax rate of 30.8%); deny deductions associated with moving jobs offshore; strengthen anti-inversion regulations Create 10% advanceable "Made in America" tax credit applicable to certain qualifying expenses such as those incurred to return production back to the US, revitalize closed or closing manufacturing plants, and incrementally increasing wages paid to US manufacturing workers Establish "claw-back" provision requiring a company to return public investments and tax benefits when they offshore US jobs

Source: Biden for President website; Biden campaign speech, Sept. 9, 2020

What’s on the table for tax policy under President Biden?

Business tax proposals

	Current law	Biden proposals
Fossil fuels and alternative energy	Intangible drilling costs 100% deductible in 1st year for independent producers and 70% deductible for integrated firms Tax exemption of set percentage of taxable income for independent oil, gas and coal producers (and investors) (“percentage depletion”) 26% investment tax credit (ITC) for qualifying projects, phasing down to 22% in 2021 and 10% in 2022 (permanently remains at 10% for geothermal and solar in 2022, completely phased out for remaining section 48 incentives)	Repeal current tax incentives for fossil fuels Expand and make permanent enhanced tax credits for renewables, such as solar
Real estate	Like-kind exchanges limited to real property $25k exemption from passive activity loss rules for rental losses Certain accelerated depreciation rules	Has called for eliminating “unproductive and unequal tax breaks” for real estate investors with income >$400k (possibly by repealing like-kind exchange rules)

Source: Biden for President website; “Biden’s $775B plan paid for with real estate taxes,” by Tyler Pager, Accounting Today (July 21, 2020)

What's on the table for tax policy under President Biden?

Business tax proposals

	Current law	Biden proposals
Pharmaceuticals	None specific to industry	Impose tax penalty on companies that raise drug costs by more than rate of inflation Repeal deduction for direct-to-consumer advertising expenses
Economic development	Opportunity Zones allow tax-free capital gains for investments held at least 10 years, basis increase for investments held at least 5 years, and temporary deferral of capital gains on existing assets placed in OZ funds New Markets tax credit for up to 39% of cost to invest in low-income community businesses, through 2020 Low Income Housing tax credit to incentivize development and improvement of affordable rental housing; an increased ceiling exists through 2021	Enhance Opportunity Zone program's accountability and transparency Expand NMTC and LIHTC and make NMTC permanent Establish Manufacturing Communities tax credit for five years to incentivize qualified investment in communities affected by mass job losses
Financial institutions	No provision	Impose risk fee on certain liabilities of financial institutions with >$50B in assets

Source: Biden for President website

What's on the table for tax policy under President Biden?

Business tax proposals

	Current law	Biden proposals
Ordinary income	Top rate of 37% through 2025 Additional 0.9% Medicare income tax applies to earned income >$200k single filer/$250k joint	Restore top rate to 39.6% for those with income >$400k
Itemized deductions	Taxpayer may deduct greater of 1) standard deduction, or 2) sum of the itemized deductions, with no cap (Pease limitation) on latter through 2025 Deduction for state and local tax (SALT) payments of up to $10k; cap expires after 2025	Restore Pease limitation for those with income >$400k Cap value of itemized deductions at 28% No specific proposal on the SALT deduction cap
Capital gains and dividends	20% tax rate applies to long-term capital gains and qualified dividends 3.8% tax on net investment income for those earning >$200k single filer/$250k joint Exclusion from capital gains tax for up to $250k single filer/$500k joint on qualifying home sales	Tax at ordinary rates for those with income >$1M
Carried interests	Treated as long-term capital gain if held for more than three years	Tax at ordinary rates

Source: Biden for President website; "Understanding Joe Biden's 2020 tax plan," Committee for a Responsible Federal Budget (July 30, 2020)

What's on the table for tax policy under President Biden?

Business tax proposals

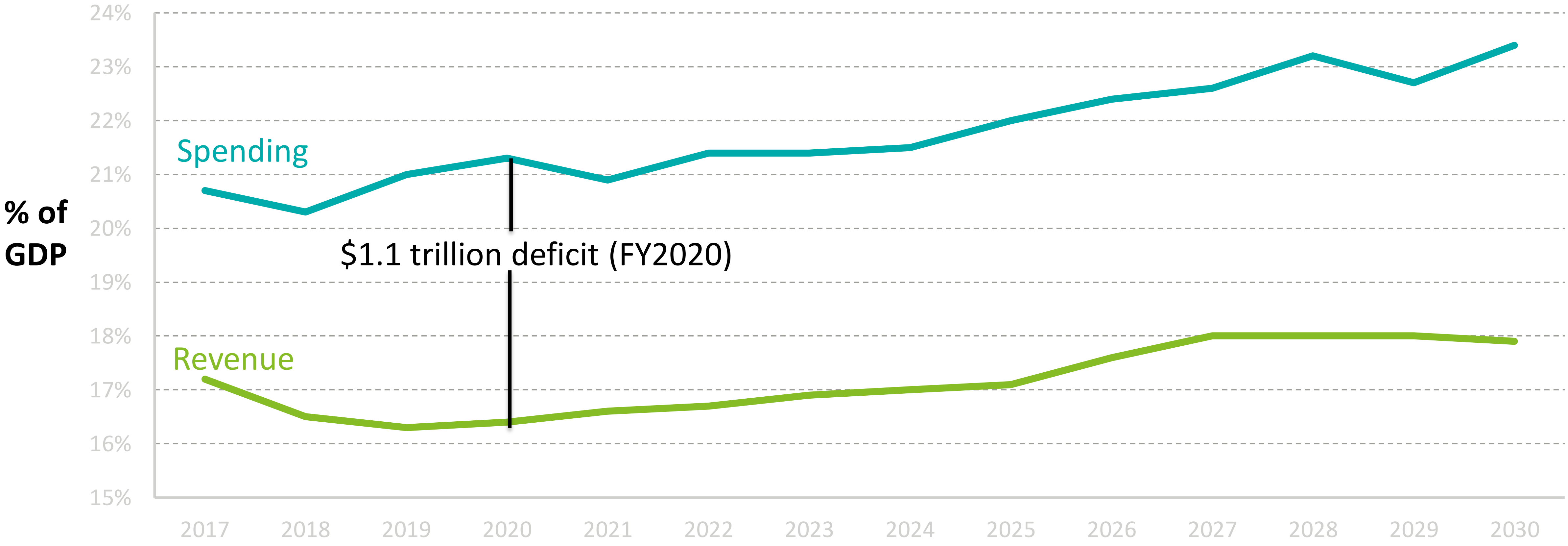
	Current law	Biden proposals
Payroll taxes	Social Security: 12.4% tax equally split between employers and employees on first $137,700 of wages (2020 cap, indexed for inflation) Medicare: 2.9% tax equally split, with no income limit S corp. profit distributions not subject to payroll tax	Expand Social Security payroll tax to apply to wages >$400k, creating a "doughnut hole" of untaxed wages between $137,700 and $400k; unclear if $400k threshold would be indexed for inflation
Passthrough income	Generally taxed at owner's individual rate, subject to 20% deduction under §199A through 2025	Phase out §199A deduction for those with income >$400k
Estate tax	40% estate, gift and generation-skipping tax; basic exemption of $10M/taxpayer, adjusted annually for inflation ($11.58M in 2020) through 2025 Step-up in basis applies to inherited assets	Has called for "returning the estate tax to 2009 levels," implying a 45% top rate and base exclusion of $3.5M per taxpayer, indexed annually for inflation Repeal stepped-up basis at death

Source: Biden for President website; "Biden to target tax-avoiding companies with minimum federal levy," by Jennifer Epstein, Bloomberg (Dec. 4, 2019)

The fiscal picture Biden will inherit: From bad to worse?

Fiscal outlook was bleak even before COVID-19 upended the economy

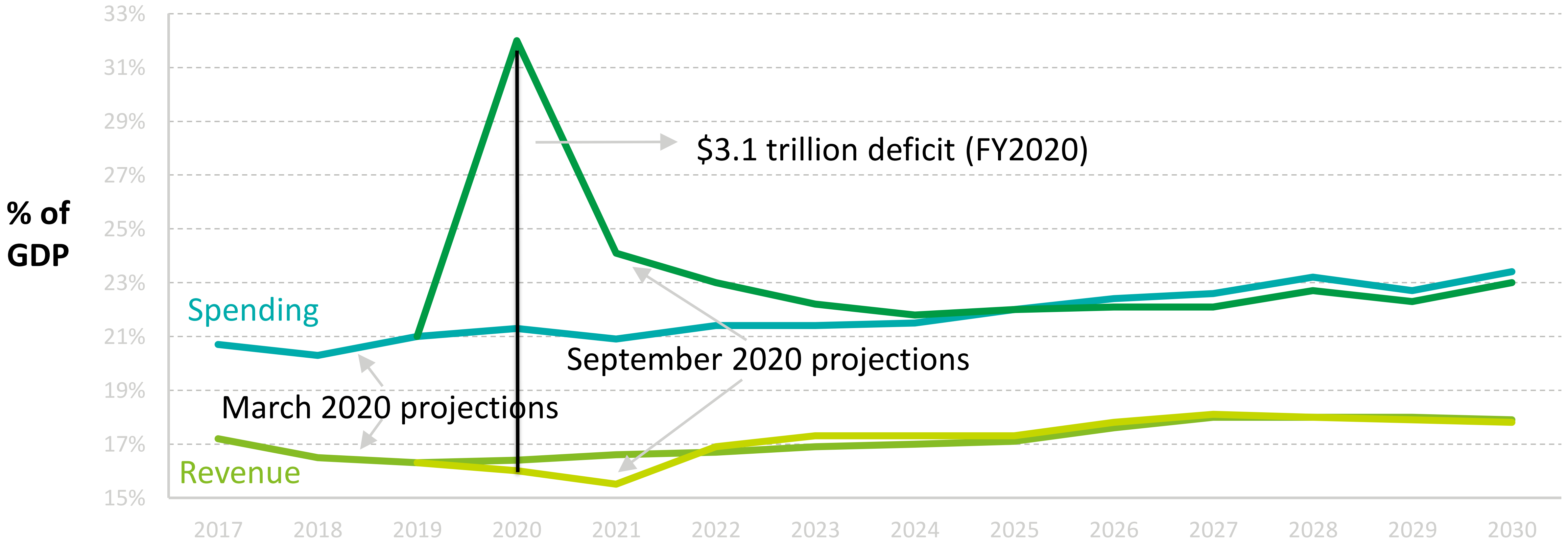
Congressional Budget Office projections from March 2020



Note: All figures reflect "current law" at the time of estimation (e.g., temporary TCJA policy lapses as scheduled, tax extenders remain expired after they lapse, etc.)
Sources: Congressional Budget Office, Baseline Budget Projections As of March 6, 2020 (Mar. 2020)

Recent fiscal projections accounting for impact of COVID-19 show spike in near-term deficits

Congressional Budget Office projections from September 2020



Note: All figures reflect "current law" at the time of estimation (e.g., temporary TCJA policy lapses as scheduled, tax extenders remain expired after they lapse, etc.)
Sources: Congressional Budget Office, Baseline Budget Projections As of March 6, 2020 (March 2020); An Update to the Budget Outlook: 2020 to 2030 (Sept. 2020)

FASB Standard Setting Update

Recent accounting developments

Recently Issued ASUs – 2020

Accounting Standards Updates ("ASUs") issued in 2020
ASU 2020-01, Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815)—Clarifying the Interactions between Topic 321, Topic 323, and Topic 815 (a consensus of the FASB Emerging Issues Task Force)
ASU 2020-02, Financial Instruments—Credit Losses (Topic 326) and Leases (Topic 842)—Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 119 and Update to SEC Section on Effective Date Related to Accounting Standards Update No. 2016-02, Leases (Topic 842) (SEC Update)
ASU 2020-03, Codification Improvements to Financial Instruments
ASU 2020-04, Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting
ASU 2020-05, Revenue from Contracts with Customers (Topic 606) and Leases (Topic 842): Effective Dates for Certain Entities
ASU 2020-06, Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity's Own Equity (Subtopic 815-40): Accounting for Convertible Instruments and Contracts in an Entity's Own Equity

Recently Issued ASUs – 2020 continued

Accounting Standards Updates ("ASUs") issued in 2020 continued
ASU 2020-07, Not-for-Profit Entities (Topic 958): Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets
ASU 2020-08, Codification Improvements to Subtopic 310-20, Receivables—Nonrefundable Fees and Other Costs
ASU 2020-09, Debt (Topic 470): Amendments to SEC Paragraphs Pursuant to SEC Release No. 33-10762
ASU 2020-10, Codification Improvements
ASU 2020-11, Financial Services – Insurance (Topic 944): Effective Date and Early Application

Recently Issued ASUs – 2020 (cont.)

ASU 2020-01

- Issue 1: An entity that applies the ASC 321 measurement alternative should consider observable transactions that require it to either apply or discontinue the equity method immediately before applying or after discontinuing ASC 323
- Issue 2: An entity should apply ASC 321 rather than ASC 323 to account for forward contracts and purchased options to acquire an equity instrument that do not meet the definition of a derivative under ASC 815

Clarifying the interactions between ASC 321, ASC 323, and ASC 815

ASU 2020-02

- Amended SEC paragraphs in the Accounting Standards Codification to Reflect the issuance of SEC Staff Accounting Bulletin No. 119 related to the new credit losses standard
- Updated SEC section to reflect comments made by the SEC staff related to the revised effective date of the new lease standard

Amendments to SEC paragraphs in ASC 323 and ASC 842

ASU 2020-03

- Codification improvements related to various aspects of the financial instruments guidance, including CECL
- Transition varies, with some of the amendments effective upon issuance for certain entities

Codification improvements to financial instruments

Recently Issued ASUs – 2020 (cont.)

ASU 2020-04 (ASC 848)

- Issued on March 12, 2020.
  - Effective date: can be adopted upon issuance and applied prospectively.
  - Temporary relief: accounting relief generally sunsets after December 31, 2022.
- Created ASC Topic 848, *Reference Rate Reform*. Primary areas of the guidance cover the following:
  - *Contract Modification* (ASC 848-20)
  - *Hedging — General* (ASC 848-30)
  - *Fair Value Hedges* (ASC 848-40)
  - *Cash Flow Hedges* (ASC 848-50)

Recently Issued ASUs – 2020 (cont.)

ASU 2020-04 (ASC 848) (cont.)

- Applies to all entities.
- ASC 848-10-15-3:

  "The guidance . . . shall apply to contracts or other transactions that **reference the London Interbank Offered Rate (LIBOR)** or a **reference rate that is expected to be discontinued** as a result of reference rate reform."

- An expectation that a reference rate will be discontinued could be supported by:

  a. **A public statement or publication** of information by or on behalf of the administrator of the relevant reference rate or by the regulatory supervisor for the administrator.

  b. **Initiatives [undertaken]** by a significant number of market participants or by market participants representing a significant number of transactions to move away from the reference rate.

  c. **The production method** for the calculation of the published reference rate [being] either:

     1. **Fundamentally restructured**

     2. **Reliant on another rate that is expected to discontinue**. [ASC 848-10-15-4; emphasis added]

Recently Issued ASUs – 2020 (cont.)

ASU 2020-06

- Simplifies an issuer's accounting for convertible instruments and contracts on an entity's own equity
- Convertible instruments
  - Separation models and expanded disclosure requirements
- Contracts on an entity's own equity
  - Equity classification conditions
- Earnings per share (EPS)
  - Diluted EPS for convertible instruments requires the if-converted method
  - Cannot rebut the presumption of share settlement for purposes of calculating diluted EPS

Accounting for convertible instruments and contracts in an entity's own equity

ASU 2020-05

- Defers the effective date of ASC 606 and ASC 842 for certain entities
  - Private companies
  - Private not-for-profit organizations
  - Certain public not-for-profit organizations
- Board will continue to evaluate effective dates of other standards
- ASC 606
  - Annual reporting periods beginning after December 15, 2019
- ASC 842
  - Annual reporting periods beginning after December 15, 2021

ASC 606 and ASC 842 effective dates for certain entities

Polling question

Has your Company already adopted ASC 842?

- Yes
- No

ASU 2020-05 Key Reminders on Deferred Standards - the “Big Picture”

ASC 606 Overview – The 5-Step Model

Core principle: Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration the entity expects to be entitled in exchange for those goods or services.

Step 1	Step 2	Step 3	Step 4	Step 5
Identify the contract with a customer	Identify the performance obligations in the contract	Determine the transaction price	Allocate the transaction price to performance obligations	Recognize revenue when (or as) the entity satisfies a performance obligation

This revenue recognition model is based on a control approach, which differs from the risks and rewards approach applied under legacy U.S. GAAP.

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ASU 2020-05 Key Reminders on Deferred Standards - the “Big Picture”

Key takeaways of the lease standard

Most leases on balance sheet for lessees

- *Classification will drive expense profile*

Lessor model

- *Most changes result from alignment with ASC 606*

FASB tried to make things easy

- *Classification, reassessment, transition*

Effective 2019 (PBE) or 2022 (non-PBE), but don’t wait to assess impact

- *Process and systems changes may be required*
- *Potential impact on debt covenants*

Recently Issued ASUs – 2020 (cont.)

ASU 2020-07

- Requires NFPs to present contributions of nonfinancial assets as its own line item separate from contributions of cash and other financial assets in the statement of activities
- Requires increased disclosure regarding contributed nonfinancial assets including types of nonfinancial assets, whether the assets were monetized, the presence of donor restrictions and valuation techniques used to measure the contributions.

Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets

ASU 2020-08

- This specific Update clarifies that for each reporting period an entity should reevaluate whether a callable debt security contains a premium to be amortized.
- Improvements are not expected to have a significant effect on current accounting practice but rather to provide additional clarity.

Codification Improvements to Subtopic 310-20, Receivables – Nonrefundable Fees and Other Costs

ASU 2020-09

- Amendments to disclosures about guarantees and issuers of guaranteed securities

Amendments to SEC Paragraphs Pursuant to SEC Release No. 33-10762

Recently Issued ASUs – 2020 (cont.)

ASU 2020-10

- Ensures proper inclusion of existing guidance in the Disclosure Section (Section 50) and the Other Presentation Matters Section (Section 45).
- Contains codification improvements related to 12 narrow scope issues. Amendments correct cross reference errors, ensure consistent use of defined terms, etc.

Codification Improvements

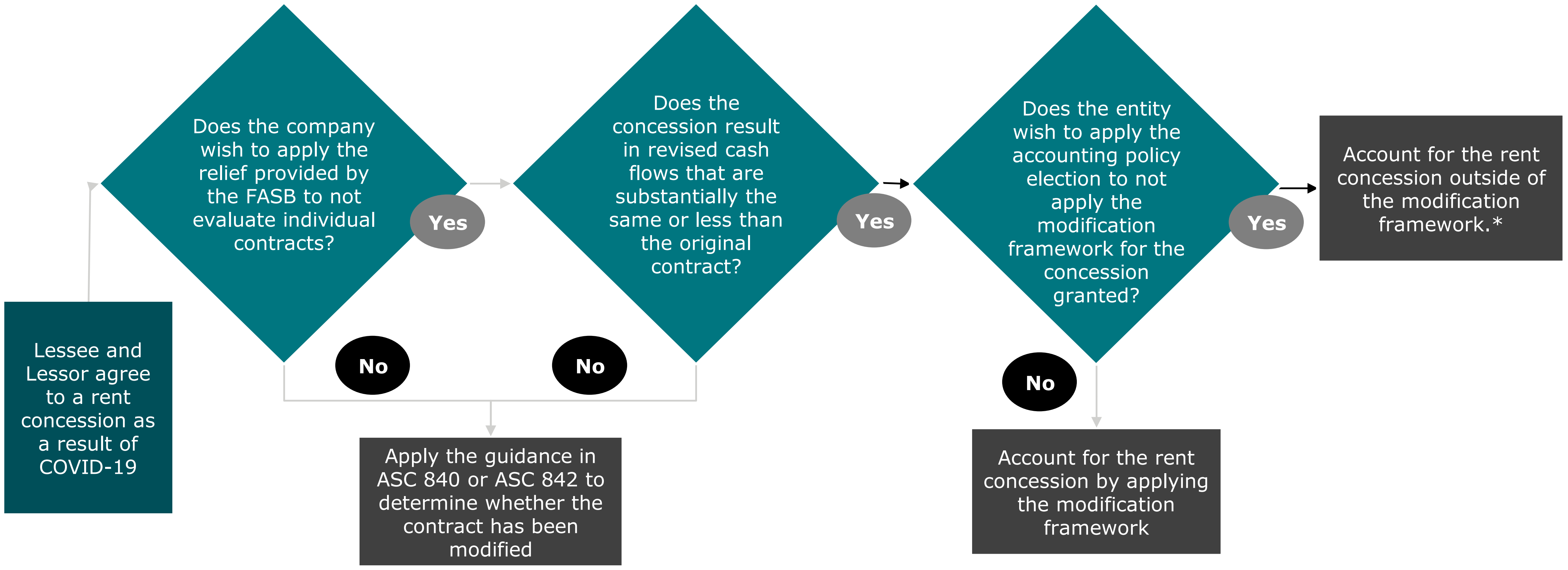
ASU 2020-11

- In 2018 the Board issued ASU 2018-12, *Financial Services – Insurance (Topic 944): Targeted Improvements to the Accounting for Long-Duration Contracts (LDTI).* The ASU's requirements included the following:
  - More frequent review and update of assumptions
  - Market risk benefits associated with deposit contract must be measured at fair value
  - Simplification of the amortization of deferred acquisition costs
  - Enhanced Disclosures
- ASU 2020-11 resets the effective date of ASU 2018-12 to be effective for fiscal years beginning after 12/15/2022 or after 12/15/2024 depending on filing status.

Financial Services – Insurance (Topic 944): Effective Date and Early Application

Leases — Modification considerations — Tenant reliefs (rent concessions)

Though not an official ASU, at the April 8 Board meeting, the FASB provided for the application of accounting policy elections related to lease modifications as a result of COVID-19



* Entities should consult with their accounting advisor regarding the acceptability of the model applied to account for the concession when not applying the modification framework.

Summary of lessee approaches

This is not a comprehensive list of all acceptable approaches. Depending on specific facts and circumstances, some or all of the approaches outlined may be applicable.

	Payable Approach	Resolution of a Contingency Approach	Variable Lease Expense Approach
Remeasure lease liability and ROU asset	✗	✓	✗
Change in straight-line lease expense	✗	?	✗
Extinguish lease liability during concession period	✗	✗	✓
FS impact during the concession period relative to absent the concession	↑ Balance Sheet	△ Balance Sheet (and sometimes Income Statement)	↑ Income Statement

? = it depends

Summary of lessor approaches

Acceptable approaches for lessors include:

- Variable lease income approach – recognize changes in payments as variable lease income in the period the change occurs
- Receivable approach – Income statement remains unchanged. Lease receivable increases during deferral period and decreases during repayment period
- Recognition of interest income on sale-type or direct financing leases
  - View A – Recognize interest income evenly over the term by calculating a new prospective effective interest rate
  - View B – do not recognize interest income during the deferral period and recognize again when payments resume

Polling question

Which new accounting standard concerns you the most going forward?

- Leases
- Revenue recognition
- CECL
- Reference rate reform
- Other

Financial reporting considerations—COVID 19

COVID-19

Financial Reporting Considerations

COVID-19 has significantly impacted the global financial markets and may have pervasive financial reporting implications for many entities, including those related to:

- Preparation of forward-looking information (estimates)
- Recoverability and impairment of nonfinancial assets
- Accounting for financial assets
- Contract modifications
- Subsequent events
- Going concern

COVID-19

Impairment of nonfinancial assets (including goodwill)

Long-lived assets

- Identification of triggering events
- Performing impairment test
  - Determining asset group
  - Undiscounted cash flows for long-lived assets – entity-based assumptions
  - Allocating impairment to assets in the group

Intangibles

- Identification of triggering events
- Performing impairment test
  - Determining fair value if impairment triggered
  - Indefinite-lived may become finite-lived

Goodwill

- Identification of reporting units
- Qualitative test
- Impairment calculation (ASU 2017-04)
- Relevance of market cap reconciliation

Costs to obtain or fulfill contracts

- Amortization approach
- Customer life / expected renewals
- Impairments

Inventory

- Lower of cost or market/net realizable value

COVID-19

Impairment of financial assets

ALLL – before adopting CECL

- Loans and receivables
- HTM and AFS debt securities

Expected credit losses – after adopting CECL

- Impact of COVID-19 on subsequent events assessment
- Impact on reasonable and supportable forecasts and pools
- HTM and AFS debt securities

Other investments

- Equity securities without readily determined fair value
- Investments in equity method investees and JVs
- Net investments in sales-type and direct finance leases
  - Adopted 842 (single model ASC 310/ASC 326)
  - Not adopted (dual model ASC 310 and ASC 360)

COVID-19

Revenue recognition

Contract existence

- Enforceability and collectibility
  - Credit risk considered as part of step one

Contract modification

- Adding goods or services at a discount
- Extending payment terms
- Granting price concessions

Variable consideration

- Updating transaction price
- Noncash consideration

Material rights

- Differentiating marketing incentives from material rights
- Extending periods over which to redeem existing rights

Recognition impacts

- Updated MOP – cost estimates and revenue estimates
- Forward losses (ASC 605-35 and ASC 605-20 contracts)

Accounting for Government Assistance

CARES Act—Accounting Framework

Assistance may come in many forms (e.g., loans, grants, tax credits, etc.)

Accounting for government assistance

Should consider the form and substance of the assistance

Consider if authoritative guidance applies such as:

- ASC 740
- Exchange transaction

US GAAP does not provide guidance on accounting for government grants to business entities

- Selection of an accounting model
  - Look to historical accounting policy
  - Consider facts and circumstances of the grant
  - Potential acceptable models may include:
    - IAS 20
    - ASC 450-30
    - Other

Accounting for Government Assistance

CARES Act—Provisions

Provisions that may include government grants, include but are not limited to:

Paycheck Protection Program (Section 1102)

Employee Retention Credit (Section 2301)

Federal Contractor Authority (Section 3610)

Pandemic Relief for Aviation Workers (Section 4112)

Public Health and Social Services Emergency Fund ($100 billion fund)

Paycheck Protection Program ("PPP")

Over $600 billion for eligible small businesses (< 500 employee per location)

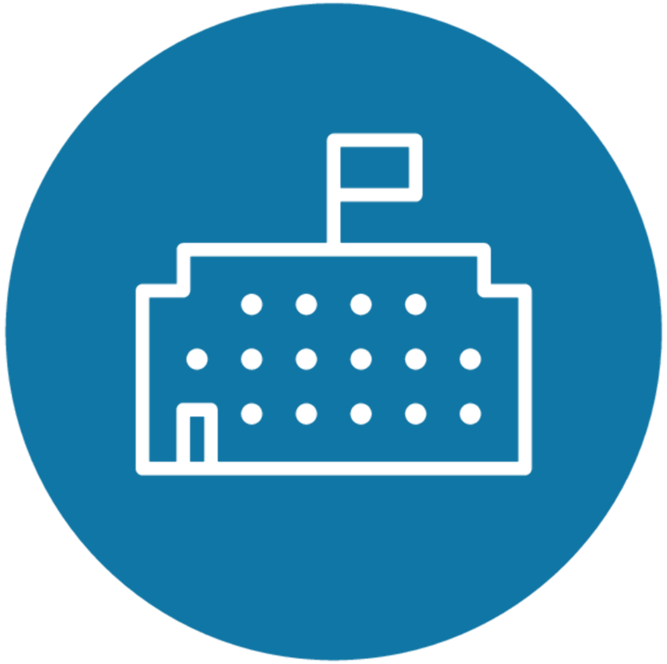
Provided assistance for certain expenses

Legal form debt

Forgiveness if conditions are met

PPP loans - Forgivable loans

- PPP loans forgivable if proceeds are used in accordance with program terms and certain criteria are met
- Important to determine compliance—expected enforcement
- Loans in excess of $2M to be scrutinized or audited
- Borrower accounting models (discussed with SEC)
  - Debt
  - Government grant
- Balance sheet, income statement, and statement of cash flows treatment may differ under each model
- Disclosures
  - Accounting policy
  - Affected line items



Polling question

Which of the following does your company find to be the most challenging?

- Forecasting results
- Accounting for contract modifications
- Impairment assessments
- Going concern assessment
- Other/not applicable

SPACs Overview

What is a Special Purpose Acquisition Company (SPAC)?

Special Purpose

- Newly formed company that raises cash in an IPO and uses that cash or the equity of the SPAC (or both) to fund the acquisition of one or more operating companies through a business combination (the "transaction"). Before completing an acquisition, SPACs hold no material assets other than cash; therefore, they are nonoperating public "shell companies"
- A SPAC has a defined life of 18–24 months to consummate an acquisition—this period can be extended up to a maximum of 36 months with shareholder approval
- If the SPAC has not consummated an acquisition by the end of its life, then it must dissolve (unless the SPAC extends its timeline via a proxy process); the SPAC returns money in the trust account to the SPAC's public shareholders, and the founder shares and warrants are worthless

Structure of SPAC

- Listed on the NYSE or NASDAQ exchange; 81% listed on NASDAQ
- IPO units have historically been priced at $10.00; IPO proceeds are held in independently run trust account. Units contain common + warrants to purchase common
- Since a SPAC does not have substantive operations before an acquisition has been completed, the target becomes the predecessor of the SPAC upon the close of the transaction, and the operations of the target becomes those of a public company As a result, the target must be able to comply with all the public-company reporting requirements that apply to the combined company. Target is considered the predecessor to an SEC registrant (i.e., the SPAC)

Transaction

- Fair Market Value of initial transaction must be at least 80% of the assets held in the trust account (excluding the deferred underwriting discount and taxes payable on the interest earned in the trust account); in reality the acquisitions are typically 2x-4x the size of SPAC
- Typically require Board and shareholder approval to consummate an acquisition

Historical and current landscape

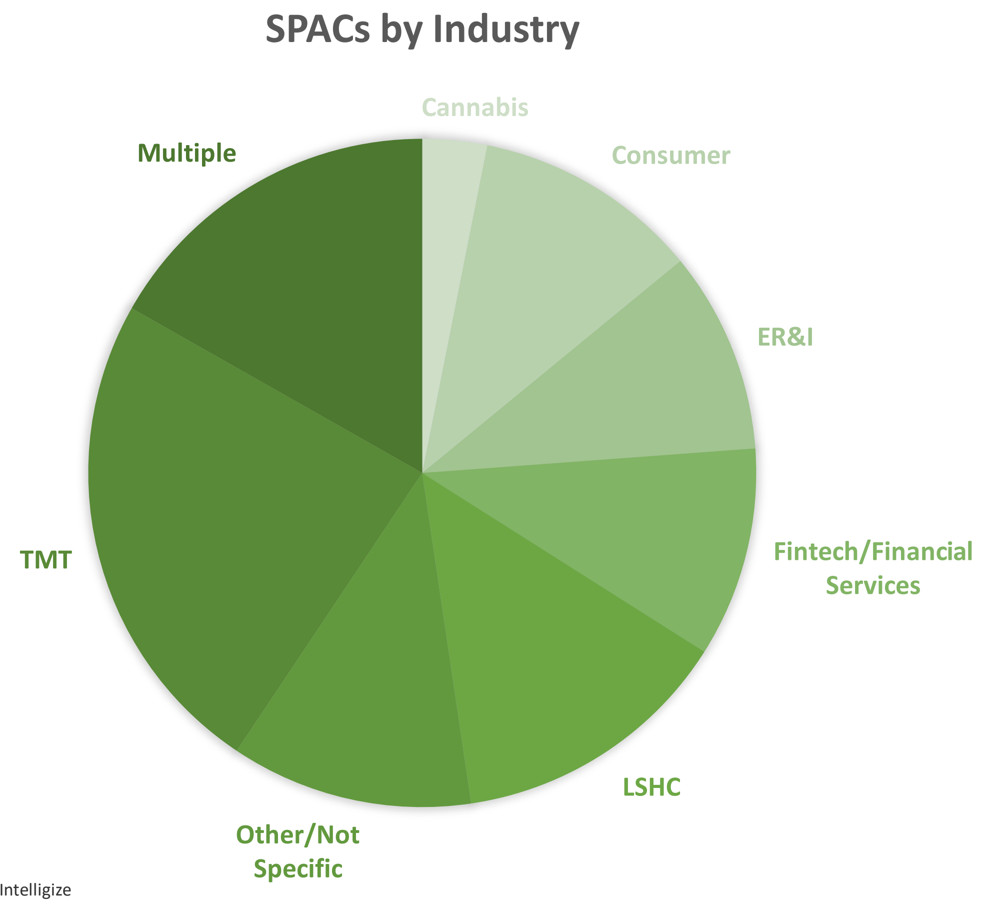
	SPAC IPO Count	Gross Proceeds ($M)	Average IPO Size ($M)
2016	13	$3,499	$269
2017	34	$10,049	$296
2018	46	$10,752	$234
2019	59	$13,600	$231
2020 (YTD)	201	$69,595	$366

Source: SPAC Insider (as of 12/1/20)

Time Left to Complete an Acquisition	# of SPACs
Less than 6 months	41
6-12 months	36
13–18 months	41
19–24 months	133
Total	**251**

Source: SPAC Research (as of 12/1/2020)

As of 12/1/20 there are **251 SPACs** yet to complete an acquisition with **$79B** of funding; 120 SPAC IPOs have been filed since 9/1/2020.



Source: Intelligize

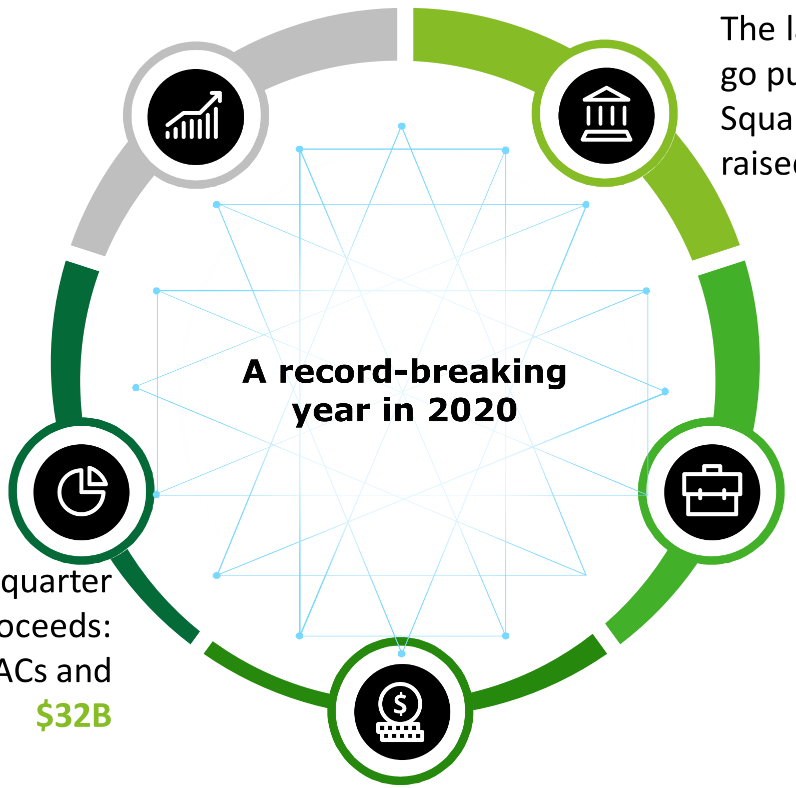
Key Trends for SPACs

Key Trends

- Additional sophisticated sponsors entering the market: Softbank, Pershing Square (Bill Ackman), Social Capital Hedosophia (3 new SPACs this year)
- Larger SPACs chasing more mature companies
- Market volatility driving a desire for more valuation certainty through a negotiation with one buyer
- Accelerated timeline to going public in uncertain times
- Success of certain “story stocks” that may not have been likely near-term IPO candidates
- Lower dilution and better alignment of sponsor incentives in some deals
- Access to PIPE capital

The most SPAC proceeds raised in a year: **$69.6B**, with 1 months to go

The largest SPAC ever to go public: Pershing Square Tontine **$4B** raised



The largest announced SPAC merger: United Wholesale Mortgage and Gores Holdings IV Inc. (**$16B**)

The biggest quarter ever by proceeds: 3Q20, 80 SPACs and **$32B**

Significant SPAC deal activity in the electric vehicle sector - **Nikola, Fisker, Canoo, Lordstown Motors, XL Fleet and ChargePoint**

Source: SPAC Research

SPAC Life Cycle[1]

Formation

- Sponsors pay nominal amount in exchange for Founders' stock ("Promote")
- Sponsors lend $100–200k to fund expenses
- Choose counsel and underwriter

IPO

- File Form S-1 with SEC, like an operating company
- 2–3 months SEC review process
- Raise money from institutional and retail investors
- Sponsors buy "at risk" warrants (2–3% of IPO proceeds)
- Almost all of IPO proceeds placed in Trust (98–100%)
- Offering expenses (underwriters, legal, audit etc.) paid out of IPO proceeds
- Units, common stock and warrants trade in market

Target Search

- Search for target—value must be at least 80% of SPAC's funds held in trust
- Sponsors reimbursed by SPAC for deal-hunting expenses out of interest earned by the trust
- Trust announces definitive agreement and begins communication with investors
- Warrants trade in market

Stockholder Vote

- File proxy with SEC (2–4 month review) and mail to shareholders in advance of vote
- Reposition stock with ongoing fundamental investors
- Vote must meet pre-specified shareholder approval threshold (60–80%)
- Dissenting shareholders have right to claim their pro rata share of trust
- "Yes" vote: acquisition closes
- "No" vote: trust (including interest earned) liquidated and returned to investors

Acquisition Close

- SPAC becomes normal operating company
- Sponsors' "Promote" crystallized (subject to lock-up)
- Sponsors' warrants crystallized (subject to lock-up)

Formation	IPO	Target Search	Stockholder Vote		Acquisition Close
2–4 months		12+ months	3–6 months		
• Team and Board appointments • Investment Strategy • Retain advisors • Pre-IPO investment	• Background checks • S-1 filing • Roadshow • Initial Public Offering	• Target evaluation • Due diligence • Negotiations and binding agreement	• Testing the Waters process • PIPE/debt financing	• Proxy filing • Super 8-K filing (4 days following close)	• Transaction close • Warrants redemption • Common stock redemption

1 = This is a general timeline. Actual timeline will depend on facts and circumstances.

Initial Public Offering vs Special Purpose Acquisition Company

Traditional Initial Public Offering (IPO)	Special Purpose Acquisition Company (SPAC)
Public market for exit	Public market for exit
Time intensive, multiple key investors, pitched via roadshow	Though time intensive, generally quicker and more efficient means to go public for the target. Companies deal with one investor rather than completing a roadshow
Generally more valuation risk and less price certainty as dependent upon market demand	Generally less valuation risk, upfront price certainty as valuation is determined by negotiation between SPAC seller and sponsor
Underwriters typically receive a discount of 1%–7% of the gross IPO proceeds	Typical discount structure is 2% of gross proceeds to be paid to underwriters at closing of IPO, with another 3.5% deposited into trust account and payable to underwriters on the closing of De-SPAC transaction; if no De-SPAC transaction takes place, 3.5% discount is never paid to underwriters and is used with the rest of the trust account balance to redeem public shares. Potential to pay more investment banking fees for the merger with the company
Requires SEC filings, review, and disclosures and public company PCAOB financial statements	Requires SEC filings, review, and disclosures and public company PCAOB financial statements

Umbrella Partnership Corporations (“Up-C”)

How to facilitate an Up-C transaction

- Form a new entity organized as a corporation (PubCo), the shares of which will be sold to the public in an IPO
- Use PubCo’s IPO proceeds to acquire an interest in the existing partnership

Tax **receivable agreement**

- In a typical Up-C IPO, the pre-IPO owners negotiate for the right, through a tax receivable agreement (“TRA”), to receive payments for a portion (typically 85 percent) of tax savings the PubCo realizes arising from the exchanges

Other potential benefits

- Offers liquidity to pre-IPO owners
- Pre-IPO owners maintain voting control over the PubCo
- Can use cash, PubCo shares, or partnership units to fund future acquisitions
- Flexibility in compensating employees
- Typically contains provisions in the TRA that serve as effective antitakeover mechanisms

Potential challenges

- Maintaining partnership books & tracking partnership unit exchanges
- Addressing buildup of excess cash at PubCo due to disparity in tax rates
- Addressing financial reporting & accounting issues associated with the Up-C transaction & subsequent reporting
- Accounting for share-based payments
- Applying consolidation guidance

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Considerations for operating companies acquired by a Special Purpose Acquisition Company (SPAC)

The opportunity and challenge

Operating companies acquired by a SPAC will face multiple SEC reporting and SOX requirements prior to the close of the transaction, similar to the requirements of companies undergoing an Initial Public Offering. Below are some of the requirements to consider regarding the financial information of the operating company.

Financial statements

- Financial statements are required to be audited under PCAOB standards
- Three years of audited financial statements can be required (two years under certain conditions)
- Financial statements are required to be on a public company GAAP basis (segments, EPS, etc.)
- Quarterly financial statements are required to be reviewed (in registration statements and periodic filings)
- New accounting standards can be required to be adopted on a public entity basis
- Business acquisitions by the operating company need to be evaluated for significance under S-X 3-05, resulting in the potential requirement for pre-acquisition financial statements

MD&A and pro forma information

- Management discussion and analysis (MD&A) is required in the merger proxy, including:
  - ✓ Results of operations
  - ✓ Liquidity
  - ✓ Consideration of non-GAAP measures
- Pro forma financial statements reflecting the impact of the transaction

Internal controls (post-close)

- Management will be required to sign certifications on the effectiveness of internal controls
- An audit report on the effectiveness of internal controls could also be required, shortly after close of the transaction

Representative timeline

The timeline from deal announcement to deal close can vary greatly based on the readiness of the operating company, however, they can potentially be as fast as 4-6 months, as shown in the following example timeline:

Transaction announced
File merger proxy
Transaction closes
File Super 8-K
File 10-Q (45 days) / 10-K (90 days)

Diligence/ Negotiation	Registration statement preparation*	SEC comment period		SOX implementation period
1-2 months	*2-4 months*	*2-4 months*	*4 days*	*1-5 years (depending on EGC status)*

* This is a general timeline. Actual timeline will depend on facts and circumstances.

Polling Question – What concerns you the most about executing a SPAC Transaction?

1. Implementing SOX Control structure
2. SEC Registration process
3. Establishing the Market Valuation of the Operating Company
4. Wait… what's a SPAC? I'm here for CPE

Question and answer

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